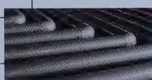
C1 ENERGY LTD.
2004 ANNUAL REPORT

UNLOCKING VALUE UNLOCKING THE LAND



C1 ENERGY LTD.

TSX: CTT

2004 ACCOMPLISHMENTS

- **Increased Oil and Gas Production and Reserves** Increased production to 750 boe/d in 2004 up from 252 boe/d in 2003 – an improvement of almost 200%. Increased total proved plus probable reserves by almost 400% and replaced our 2004 production by over 1200% on a total proved plus probable basis.
- **Improved Year Round Access** Successfully established two new, year round access, multi-zone gas exploration projects at Blueberry and Sarcee. Increased year round access from 35% to 65% across C1 assets.
- **Established New Core Development Area** Added a new core, low-risk, high-impact gas development project at Whiskey Creek through the acquisition of Extreme Energy.
- **Balanced Oil to Gas Production Ratio** Improved production mix from 80% light oil and 20% gas to 50% light oil and 50% gas.

2005 PRIORITIES

- 20 new wells planned in 2005 drilling program
- Production gains forecast at Gift Lake, Chipmunk, Blueberry, and Sarcee
- 2005 exit production target: 1,600 boe/d
- $17.0 million capital budget for 2005
- Continue high-impact exploration and development
- Target medium-depth, medium-risk light oil and natural gas
- Continue evaluation of strategic acquisitions
- Monetize proven non-producing reserves

ANNUAL MEETING

Shareholders and guests are invited to attend the Annual Meeting to be held on Tuesday, May 17, 2005 at 3:00 p.m. in the Plaza Room of the Metropolitan Conference Center, 333 – 4th Avenue S.W., Calgary, Alberta.

C1 Energy Ltd. is engaged in the exploration and development of oil and natural gas reserves in Alberta. We were founded in December 2003 and listed on the Toronto Stock Exchange in January 2004.

The Company brings together a veteran team of exploration leaders and operators with more than 100 years of exploration accomplishments in the Western Sedimentary Basin. We are utilizing a portfolio approach to unlock the value of a broad base of mixed risk assets across Alberta.

TSX: CTT

C1 ENERGY LTD.

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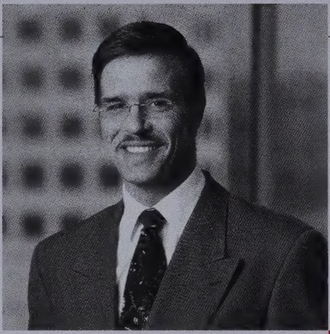


HUGH PATTILLO
PRESIDENT AND
CHIEF EXECUTIVE OFFICER

MESSAGE FROM THE PRESIDENT

2004 was the first full year of operations for C1 and it has been a year of concerted growth. Over the last 12 months, we demonstrated our ability to plan and execute the business fundamentals of an exploration company. We established our prospect inventory, successfully financed and brought on new production, and completed an acquisition synergistic to our exploration plan. From a modest production and reserve base at our inception, C1 enters 2005 with quadruple the reserves and double the production over the first year of operations.

2004 ACCOMPLISHMENTS

We are proud of our accomplishments in the first full year of operations of C1. We achieved significant growth in key aspects of our business. C1 increased production from 252 boe/d at the close of 2003 to 750 boe/d at the close of 2004 and remain on track for our 1,200 boe/d production target for the first quarter of 2005. We increased total proved plus probable reserves to 2.6 million barrels from 0.5 million barrels last year, an increase of almost 400%. Our acquisition of Extreme Energy in the Peace River Arch contributes 10,000 net undeveloped acres to our Blueberry core operating area and adds an additional 220 boe/d light oil and natural gas production. The acquisition of Extreme also equips the Company for additional year round operations and balances our oil and gas production mix.

C1 also enhanced its financial and management strength in 2004. We closed a flow-through common share financing agreement in May for total gross proceeds of $10.0 million. With this financing, the Company has $4.4 million of working capital and access to $8.5 million in credit. To help lead our growth, C1 welcomed Mr. Ron Barmby P. Eng., M. Eng. as Vice President and Chief Operating Officer, and Mr. Bill VanderVeen, P.Geol., as Vice President Exploration, adding depth to the operating and exploration capability of our management team.

OPPORTUNISTIC BUT COMPETITIVE MARKET

Within Alberta's oil and gas industry, market attention, commodity prices and access to capital are at a record high, as is competition among an ever-increasing population of junior exploration companies. Juniors are now vying for limited growth opportunities in a maturing basin, and for a reducing number of acquisition candidates due to the proliferation of income trust conversions. For companies able to navigate these challenges and deliver strong growth through the drill bit, there has rarely been a more opportune market. C1 is uniquely positioned for this type of growth.

UNLOCKING VALUE

In 2004, C1 demonstrated its ability to plan and execute the business fundamentals of an exploration company. In its first full year in operations, the Company established its prospect inventory, successfully financed and brought on new production, and completed an acquisition synergistic to its exploration plan.

FUNDAMENTAL STRENGTHS OF C1 ENERGY

C1 has over 300,000 net acres of land inventory in proven productive regions, and in over half of this land base we operate with minimal competition due to exclusive access arrangements. We have an inventory of more than 60 drilling locations, which represent a balanced mix of low, medium and high-risk targets for high netback light oil and natural gas. The Company also has an exploration team with proven capability to generate and recognize economic opportunities for new plays on existing lands and in new areas of the Western Canadian Sedimentary Basin.

2005 OUTLOOK

We anticipate the next year will be one of significant growth for C1. The Company has a $17.0 million capital program in place, and we are aiming to drill more than 20 wells in 2005 as we continue exploiting our asset base. We have a production target of 1,600 boe/d exiting the year, and production gains will begin to come on stream throughout 2005 and into 2006. We will also continue to evaluate strategic acquisitions that are complementary to our exploration strategy and core areas of operations.

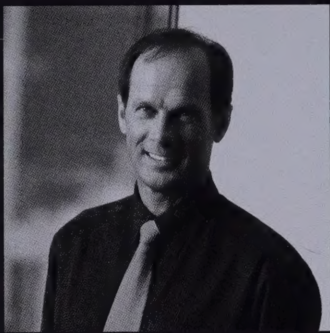
In 2004, C1 began demonstrating the promise of our mixed risk portfolio strategy of unlocking the value of our extensive land and asset base. We remain focused on this strategy as we enter 2005 and are on course to generate the strong results that will help build a sustainable and profitable company. There is plenty of work ahead and we will take it on with discipline and determination.

I would like to thank the staff and Board of Directors of C1 for the work and dedication to our Company through our first year of operations. The most important asset of any company is its people, without which the ideas and their execution would not be possible.

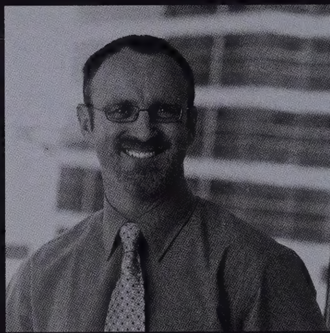
On behalf of the Board, the management of C1 would like to thank the Company's shareholders for their support. We are very confident in C1's prospects for the coming year and believe our shareholders will begin to realize the rewards of their confidence in the Company's strategy and leadership in 2005.

On behalf of the Board of Directors,

Hugh Pattillo
President and Chief Executive Officer
March 28, 2005



RON BARMBY
VICE PRESIDENT AND
CHIEF OPERATING OFFICER

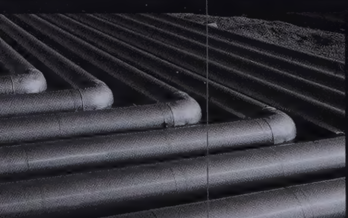


GARY LOBB
VICE PRESIDENT OF FINANCE
AND CHIEF FINANCIAL OFFICER

BILL VANDERVEEN
VICE PRESIDENT OF EXPLORATION

- Over 300,000 net acres of land inventory in proven producing fairways
- Over 60 drilling locations at light oil and natural gas targets
- Mixed risk portfolio unique for a junior exploration company

PROPERTY OVERVIEW



C1's exploration and development program is focused in the Peace River Arch, the W5 Central Alberta region and Northern Alberta. Our asset base consists of over 136,000 net acres of undeveloped lands in proven producing fairways. We have agreements on exclusive access or farm-in to an additional 178,000 net acres of undeveloped lands for a total land inventory of over 314,000 net acres.

C1 has identified over 60 drilling locations on our land base, which give us exposure to multi-zone light oil and natural gas targets that represent a mix of low, medium and high-risk opportunities. This mixed risk portfolio is unique for a junior exploration company, and presents significant opportunity for reserve and production growth for our shareholders. We continue to build on our existing land and opportunity base.

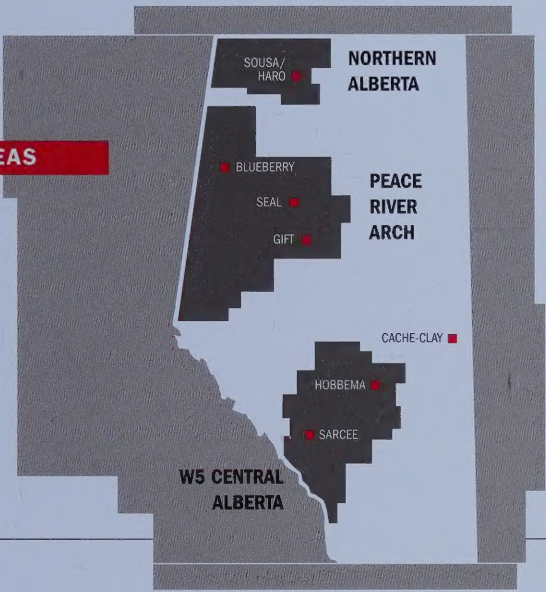
2005 CAPITAL BUDGET BY CORE AREA

TOTAL 2005
CAPITAL BUDGET
$17.0 MILLION

UNLOCK THE LAND

C1 possesses a broad base of mixed risk assets in the Peace River Arch, Central Alberta and Northern Alberta. C1 is the majority owner and operator of 136,000 net acres of undeveloped land with over 60 drill-ready locations. Our assets represent 6,500 boe/d unrisked production upside and 6.4 mmbbls unrisked potential reserves upside.

CORE AREAS



NORTHERN ALBERTA
- Average 88% working interest, 66% operations control
- Key assets: Haro
- Prospect mix – 100% gas
- 17 drilling opportunities
- 12% capital budget allocated 2005

PEACE RIVER ARCH
- Average 86% working interest, 100% operations control
- Key assets: Gift, Seal, Blueberry
- Prospect mix – 46% oil and 56% gas
- 35 drilling opportunities
- 76% capital budget allocated 2005

W5 CENTRAL ALBERTA
- Average 70% working interest, 50% operations control
- Key assets: Hobbema, Sarcee
- Prospect mix – 100% gas
- 12 drilling opportunities
- 12% capital budget allocated 2005

PEACE RIVER ARCH

- Gift Lake waterflood producing 190 bbls/d at end 2004, 375-450 bbls/d targeted for 2005
- New exploration drilling in 2004 at Chipmunk netted 1.3 mmcf/d gas production, 1.5 mmcf/d to be tied in during 2005
- Peace River Arch remains a prime exploration region

GIFT LAKE EXPLORATION AND DEVELOPMENT

Gift Lake is one of our key exploration properties and C1 operates 100% of the production from this area. The property is located approximately 250 kilometres northwest of Edmonton, Alberta in an area that is characterized by prolific, long life, high netback light oil and gas production. C1 began to realize the substantial value of Gift Lake in 2004, exiting the year with 444 boe/d from the area, comprising 58% of our total production.

The Gift Lake area has 60% year round access with both long life high-quality light oil production and long life sweet, dry natural gas production. C1 has exclusive access to surface rights and the exploration potential of a further 168,000 acres of undeveloped lands. C1 has an inventory of 24 drilling locations, both development and exploration, in this area that are identified by an extensive base of 2D and 3D seismic. We have evaluated approximately only 12% of the lands with 3D seismic.

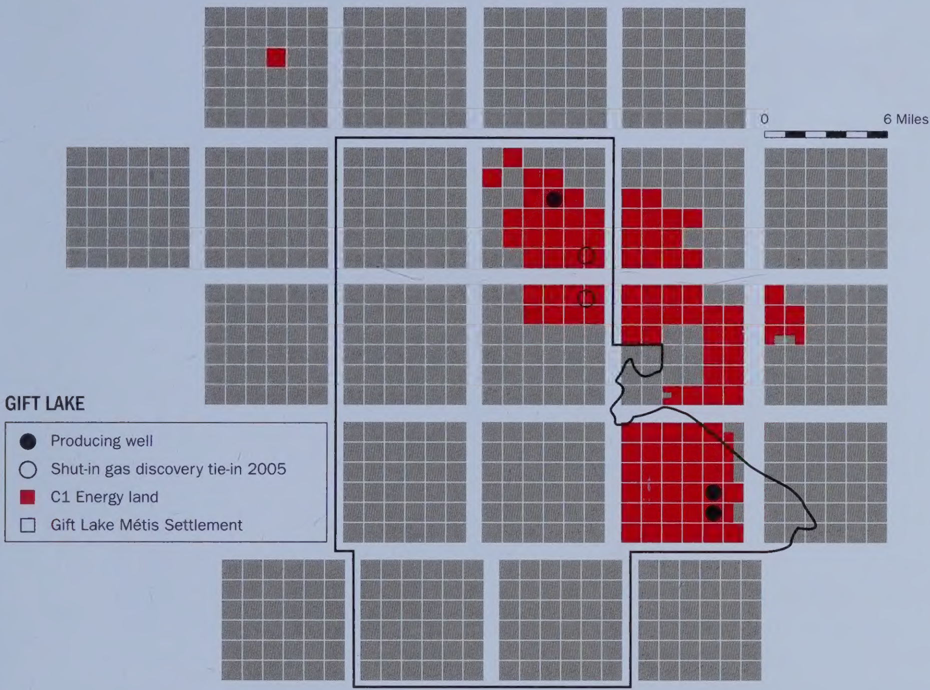
C1 expects to spend 34% of its capital budget on our Gift Lake projects in 2005.

GIFT LAKE – "G"POOL

C1 holds a 75% working interest in Gift Lake oil production. We initiated a waterflood project in the fourth quarter of 2004 and exited the year producing approximately 190 bbls/d from these two wells. Management estimates the pool to have 3.0 million to 5.0 million barrels of light, sweet oil in place. The waterflood enables us to potentially recover between 25% to 40% of the in-place reserves. We expect production to increase to 375-450 bbls/d net to C1 over the course of 2005 and beyond, now that we have received GPP approval from regulatory authorities.

C1 had a 342% increase in the total proved plus probable reserves assigned to this property in 2004 indicating the reserve and production potential. The full reserves potential associated with this pool will be recognized over the next several years as production performance continues to verify our internal reserve assessment. Production from this property comprised 27% of C1's total production and 32% of C1's total proved plus probable reserves at year-end.

C1 has approximately 117 square kilometres of 3D seismic coverage over this area that has identified numerous similar features to the "G" Pool. Now that the viability of waterflood has been proven in the "G" Pool, we will begin a medium-risk exploration program of the first of these prospective pools in 2005. We will extend this medium-risk exploration program to the northeast in the third quarter as we begin to further evaluate the play fairways that have been identified to date.



GIFT LAKE – CHIPMUNK

The Chipmunk Shallow Gas project is located on the north end of the Gift Lake Settlement. At the beginning of 2004 the area had one standing gas well with no production. Successful exploration drilling by C1 and strong production from a newly tied-in well resulted in 1.3 mmcf/d of net production in 2004 with 2.0 mmcf/d (1.5 mmcf/d net to C1) of gas production awaiting tie-in during the first quarter of 2005. We currently have an inventory of three to seven drilling locations in the area and we will continue to extend the play through drilling, pipeline construction and tie-in operations in 2005. The new wells drilled in 2004 are estimated to represent 1.5 mmcf/d to 2.0 mmcf/d of gross productive capacity to C1 (188-250 mboe/d net C1). With further facility and development projects, production levels could reach 4.0 mmcf/d to 5.0 mmcf/d (415-520 boe/d net) from this area by the end of 2005.

C1 had a 490% increase in the total proved plus probable reserves for this property in 2004. Production from this property comprised 31% of total C1 production and 21% of total proved plus probable reserves at year-end.

SEAL EXPLORATION AND DEVELOPMENT

The Seal property, located approximately 290 kilometres northwest of Edmonton, Alberta, is C1's second largest producing property. This area has total net production of 140 bbls/d of high-quality light crude. There are currently seven producing oil wells associated with this property. The oil and associated gas production comes from Devonian aged Slave Point Reefs at a depth of 1,800 metres. C1 is the operator and has an average 60% working interest in the Seal area. C1 currently has two locations planned for this property in 2005.

C1 had a 31% increase in the total proved plus probable reserves for this property in 2004. Production from this property comprised 13% of total C1 production and 12% of total proved plus probable reserves at year-end.

C1 expects to spend approximately 8% of its capital budget in the Seal area in 2005.

PEACE RIVER ARCH

BLUEBERRY EXPLORATION AND DEVELOPMENT

The Blueberry area is located approximately 500 kilometres northwest of Edmonton and is C1's newest exploration area. We had, prior to the acquisition of Extreme Energy, a 50% working interest in a joint venture with Extreme in this area. With the closing of the acquisition in December, our position increased to an average 67% working interest in 19 sections of land with a drilling inventory of 11 locations. C1 also has an additional 2,560 acres of land under farm-in agreements.

C1 delayed new drilling at Blueberry in 2004 to allow for the acquisition of Extreme. With the Extreme transaction, C1 added 83 boe/d from producing wells at year-end.

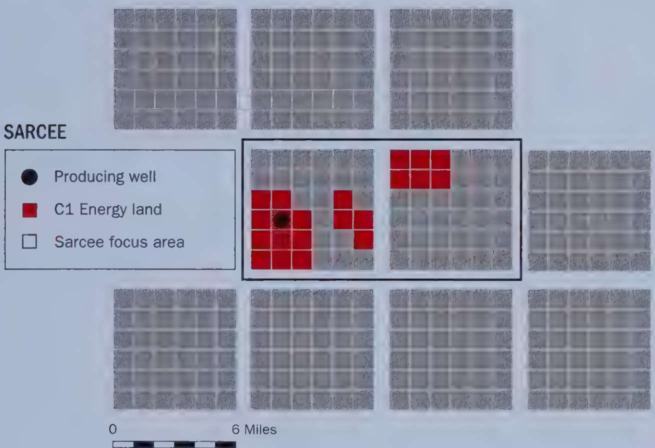
Establishing a new core area was a target of our business plan in 2004 and Blueberry accomplishes this goal, contributing year round access and multi-zone gas prospect inventory for a balanced exploration program.

The 2005 drilling program for Blueberry constitutes about 35% of our capital budget and includes seven wells targeting multi-zone gas targets, dominantly medium to high-risk with year round access. We will work to expand our prospect inventory at Blueberry in 2005 and beyond as we capitalize on the investment made through the acquisition of Extreme Energy. Our current drilling program has begun to provide our first production additions in our plan to develop this area into a core production asset.

Production from this property comprised 3% of total C1 production and less than 1% of total proved plus probable reserves at year-end.

W5 CENTRAL ALBERTA

- Acquisition of Extreme Energy gives C1 82% working interest in 17 sections of area land
- Sarcee reserves make up one-quarter C1 total reserves
- W5 region 100% gas assets



SARCEE (TSUU T'INA) EXPLORATION AND DEVELOPMENT

The Tsuu T'ina First Nation is located near the southwestern limits of Calgary. The areas adjoining the Sarcee lands have been the focus of substantial industry activity that have resulted in significant, long life gas and associated liquid production. Through the acquisition of Extreme, C1 now has an average 82% working interest in 17 sections of land on the block.

C1 completed a 3D seismic program to evaluate these properties in December 2004, and will prepare a full exploration and development program for the area pending analysis of the findings. This is the second 3D program conducted on the Sarcee lands and these have provided the technical basis for our exploration and development programs.

We have two separate operating areas on the lands. The first area is a four-section block held 100% by C1 with exploration potential defined by 3D seismic, with one proposed well location. C1 is currently in the process of finalizing drilling plans for a high impact exploration well to target a 20 bcf to 25 bcf pool with initial deliverability of 3.0 mmcf/d to 5.0 mmcf/d targeted for late in 2005. We anticipate that C1 will hold a 50% to 60% working interest in this well after drilling and completion of the well are finished.

The second area is an 11-section block on the western side of the area where C1 holds an average 76% working interest. On this block, we also hold a 50% non-operated interest in a production well in Sarcee, producing 600 mcf/d (300 mcf/d net) and 33 bbls/d (16 bbls/d net) of associated liquids. Development potential exists for a producing well with an evaluated in place reserves base of 45 bcf of raw gas plus associated liquids. Total proved plus probable reserves associated with this property comprise 25% of C1's total reserves.

C1 expects to spend approximately 10% of its capital budget on Sarcee projects in 2005.

DRILL WELLS & TIE THEM IN

C1 drilled five wells in the first quarter of 2004, with an 80% success rate. C1 doubled production through drilling. C1 exited 2004 on track to exceed its first quarter 2005 production target of 1,200 boe/d. C1 plans to drill 20 new wells in 2005.

NORTHERN ALBERTA

HARO EXPLORATION AND DEVELOPMENT

The Haro area is located 600 kilometres northwest of Edmonton, Alberta and is the focus of a joint venture agreement between C1 and an industry partner. Exploration and development drilling at Haro targets shallow gas sands. C1 will drill, case and complete five wells on these lands in the first half of 2005 to earn a 50% working interest in the reserves and shut-in production potential in three shut-in gas wells on these lands. These wells are internally estimated to have 0.5 bcf to 1.0 bcf of recoverable reserves and are recognized in our reserve report.

This area is a new focus area for C1 and represents a medium to low-risk inventory of drilling prospects. After earning into the area, we will be named the operator of the project and plans to continue drilling the currently identified 10 to 12 locations on the lands. With our partners, we will look to tie-in the standing and successful wells in the winter of 2006 when pipeline capacity is available in the area.

C1 expects to spend 10% of its capital budget on Haro projects in 2005.

OPERATIONS REVIEW

RESERVES

The following tables summarize certain information with regard to C1's oil and gas reserves as evaluated by Sproule Associates Limited as at December 31, 2004. Additional information required under NI 51-101 will be included in the Annual Information Form to be filed for fiscal 2004.

	Crude Oil		Natural Gas[1]		Natural Gas Liquids		Barrels of Oil Equivalent	
	Gross (mbbl)	Net (mbbl)	Gross (mmcf)	Net (mmcf)	Gross (mbbl)	Net (mbbl)	Gross (mboe)	Net (mboe)
Proved								
Developed producing	603.8	479.9	2,251	1,478	72.2	42.8	1051.2	769.0
Developed non-producing	54.1	47.3	33	23	1.7	1.2	61.3	52.3
Undeveloped	0.0	0.0	2,786	1,877	40.9	23.7	505.2	336.5
Total proved	657.9	527.3	5,070	3,377	114.8	67.7	1,617.8	1,157.8
Probable	420.1	328.5	3,066	2,074	92.3	54.1	1,023.4	728.3
Total proved plus probable	1,078.0	855.8	8,136	5,452	207.1	121.8	2,641.2	1,886.1

[1] Includes solution gas plus non-associated and associated gas.

SUMMARY OF NET PRESENT VALUES OF FUTURE NET REVENUE

As at December 31, 2004 ($000s)	Forecast Prices and Costs			
	Before Income Taxes Discounted at (%/Year)			
Reserve Category	0%	5%	10%	15%
Proved				
Developed producing	18,846	16,281	14,407	12,982
Developed non-producing	1,085	876	721	603
Undeveloped	5,671	4,460	3,620	2,996
Total proved	25,602	21,617	18,747	16,582
Probable	13,174	9,860	7,796	6,321
Total proved plus probable	38,776	31,477	26,544	22,903

Notes: NPV of FNR include all resource income: Sale of oil, gas, by-product reserves; Processing third party reserves; Other income.

SUMMARY OF PRICING AND INFLATION RATE ASSUMPTIONS

As of December 31, 2004 — **Forecast Prices and Costs**

	WTI Oil Cushing Oklahoma ($US/bbl)	Edmonton Oil Par Price 40° API ($Cdn/bbl)	Cromer Oil Medium 29.3° API ($Cdn/bbl)	Natural Gas[1] AECO Gas Prices ($Cdn/mmbtu)	Pentanes Plus FOB Field Gate ($Cdn/bbl)	Butanes FOB Field Gate ($Cdn/bbl)	Inflation Rate[2] (%/Year)	Exchange Rate[3] ($US/$Cdn)
Historical								
2001	25.94	39.06	31.56	6.23	42.46	27.93	2.0	0.646
2002	26.09	40.12	35.46	4.04	40.80	25.39	2.7	0.637
2003	31.14	43.23	37.53	6.66	44.16	34.55	2.5	0.716
2004	**41.41**	**52.91**	**45.72**	**6.87**	**53.90**	**41.38**	**2.5**	**0.77**
Forecast								
2005	44.29	51.25	44.53	6.97	52.49	38.20	2.5	0.840
2006	41.60	48.03	41.87	6.66	49.19	34.01	2.5	0.840
2007	37.09	42.64	37.27	6.21	43.67	30.20	2.5	0.840
2008	33.46	38.31	33.43	5.73	39.23	27.13	2.5	0.840
2009	31.84	36.36	31.70	5.37	37.24	25.75	1.5	0.840
Thereafter	Various Escalation Rate							

[1] This summary table identifies benchmark reference pricing schedules that might apply to a reporting issuer.

[2] Inflation rates for forecasting prices and costs.

[3] Exchange rates used to generate the benchmark reference prices in this table.

Notes: Product sale prices will reflect these reference prices with further adjustments for quality and transportation to point of sale.

RESERVES LIFE INDEX [1]

	Total Proved	Proved Plus Probable
Total gross reserves (mboe)	1,617.8	2,641.2
Exit production rate (boe/d)	750	750
Fourth quarter production (boe/d)	516	516
Annual 2004 production (boe/d)	501	501
RLI based on annualized exit production (years)	6.0	9.6
RLI based on annualized fourth quarter production (years)	8.6	14.0
RLI based on annual 2004 production (years)	8.8	14.4

[1] Calculated by taking total reserves divided by annualized production.

NET ASSET VALUE

The net asset value for the Company at December 31, 2004, is determined as follows:

($000s except per share amounts)	2004 Forecast Prices and Costs on Reserves	2004 Constant Prices and Costs on Reserves	2003 Forecast Prices and Costs on Reserves	2003 Constant Prices and Costs on Reserves
Present value of proved plus probable reserves (discounted at 10% before tax)[1]	$ 26,544	$ 31,711	$ 4,794	$ 5,853
Undeveloped land[2]	9,623	9,623	8,710	8,710
Lands subject to exclusive access by C1[3]	4,450	4,450	–	–
Working capital	4,468	4,468	8,981	8,981
Proceeds from exercise of stock options	2,064	2,064	–	–
Net asset value	$ 47,149	$ 52,316	$ 22,485	$ 23,544
Shares outstanding with full dilution[4]	29,014	29,014	17,757	17,757
Net asset value per share	$ 1.63	$ 1.80	$ 1.27	$ 1.33

[1] Value obtained from independent engineering evaluation.

[2] Value from independent third party evaluation dated December 31, 2004.

[3] Lands on the Gift Lake Métis Settlement covered by the AMI plus lands under the Haro JV valued at $25/acre x 178,000 net acres as determined by management.

[4] Includes 27,609,408 C1 Common Shares plus 625,000 options, 371,116 warrants and 409,000 shares on conversion of performance shares based on an average trading price of $1.94 per share.

Note: Net asset value excludes an estimated $7.5 million of seismic value in 2004 (2003 – $4.2 million).

UNDEVELOPED LAND

All of C1's undeveloped land has been evaluated by Seaton Jordan. In 2004, our undeveloped land inventory rose 11% to 136,000 net acres, an increase of approximately 14,000 acres from last year. This does not include an additional 168,000 net acres of land on the Gift Lake settlement that C1 has exclusive surface access to under an agreement with the Gift Lake Métis Settlement. All of C1's undeveloped acreage is located in Alberta.

Undeveloped Land Holdings by Region

Year ended December 31, 2004	Gross Acres	Net Acres	Average Working Interest
Peace River Arch	109,090	93,615	86%
W5M	36,428	25,617	70%
Northern	18,880	16,859	89%
Other	640	256	40%
Total	**165,038**	**136,347**	**83%**

DRILLING ACTIVITY

	Exploration		Development		Total	
Year Ended December 31, 2004	Gross	Net	Gross	Net	Gross	Net
Oil	2	1.2	–	–	**2**	**1.2**
Gas	2	1.5	–	–	**2**	**1.5**
D&A	1	1.0	–	–	**1**	**1.0**
Total	**5**	**3.7**	–	–	**5**	**3.7**

MANAGEMENT'S DISCUSSION AND ANALYSIS

C1's President and Chief Executive Officer and the Chief Financial Officer have signed a statement outlining management's responsibility for financial information in this Annual Report. The statement also explains the roles of the Audit Committee and Board of Directors in respect of financial information in the Annual Report.

The following discussion is management's assessment of the operating and financial results of C1 Energy Ltd. ("C1" or the "Company") as well as its future opportunities and risks, and should be read in conjunction with the audited financial statements and related notes of the Company for the for the year ended December 31, 2004 and the three day period from commencement of operations on December 29, 2003 and ended on December 31, 2003. The financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). The commentary is as of March 11, 2005. The reader should be aware that historical results are not necessarily indicative of future performance.

C1 commenced operations on December 29, 2003 when a portion of the assets of Navigo Energy Inc. ("Navigo") were transferred to C1. As the transfer of assets took place between related companies (at that time) the assets were transferred to C1 for financial statement purposes at book value. As such, comparisons year to year may not be meaningful and therefore where period to period comparisons are made in this discussion and analysis, they are primarily between the fourth quarter of 2004 and the third quarter of 2004, or between the fourth quarter of 2004 and the full year ended December 31, 2004.

In conformity with Canadian Securities Administrator's National Instrument ("NI") NI 51-101 "Standards of Disclosure for Oil and Gas Activities", natural gas volumes have been converted to equivalent barrels of oil ("boe") using a conversion ratio of six thousand cubic feet ("mcf") of natural gas to one boe. This ratio is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead. Readers are cautioned that boe may be misleading, particularly if used in isolation.

Non-GAAP Measurements

The MD&A contains the term "cash flow from operations" ("cash flow"), which should not be considered an alternative to, or more meaningful than, "cash flow from operating activities" as determined in accordance with Canadian GAAP as an indicator of the Company's financial performance. C1's determination of cash flow from operations may not be comparable to that reported by other companies. The reconciliation between net earnings and cash flow from operations can be found in the statements of cash flows in the financial statements. The Company evaluates its performance based on net income and cash flow from operations. The Company considers cash flow from operations to be a key measure as it demonstrates the Company's ability to generate the cash necessary to repay debt and to fund future growth through capital investment. Cash flow from operations per share is calculated using the diluted weighted average number of shares for the period.

Forward Looking Statements

This disclosure contains forward looking statements that involve substantial known and unknown risks and uncertainties, certain of which are beyond C1's control, including: the impact of general economic conditions in Canada and the United States, industry conditions, changes in laws and regulations including the adoption of new environmental laws and regulations and changes in how they are interpreted and enforced, increased competition, the lack of availability of qualified personnel or management, fluctuations in foreign exchange or interest rates, stock market volatility and market valuations of companies with respect to announced transactions and the final valuations thereof, and obtaining required approvals of regulatory authorities. C1's actual results, performance or achievement could differ materially from those expressed in, or implied by, these forward looking statements and, accordingly, no assurances can be given that any of the events anticipated by the forward looking statements will transpire or occur, or if any of them do so, what benefits, including the amount of proceeds, that C1 will derive there from.

BUDGET FOR EXPANSION

In May 2004, C1 closed a flow-through common share financing agreement, on a bought deal basis, for total gross proceeds of $10.0 million. With the financing, C1 can comfortably fund its $17.0 million Capex program for 2005. C1 has $6.9 million cash on hand, and access to an $8.5 million credit facility.

CORPORATE VISION AND STRATEGY

C1 is a Calgary based junior exploration and production company whose business plan is to create shareholder value through exploration, development, acquisition and production of oil and gas primarily in the province of Alberta. Our vision is to build a high-quality asset and production base that will generate sustainable cash flow and a profitable return to our shareholders while maintaining our core value of integrity. Our strategy for building a high-quality asset base will concentrate on finding and developing oil and natural gas through the exploration of a diversified, mixed risk, drilling portfolio while maximizing production and recoveries from our existing assets. C1 will engage in accretive acquisitions that complement our exploration activities.

Our operational objectives in carrying out our strategy have the following characteristics:

Drill primarily internally-generated exploration and development prospects;

Target areas and projects that can result in meaningful reserve and production additions;

Focus exploration efforts on multi-zone areas in order to maximize opportunities for drilling success and gain exposure to higher-risk, high-impact targets;

Explore for light oil and natural gas but opportunistically pursue other targets if they make economic sense;

Operate and maintain a majority working interest in our core areas in order to establish operating efficiencies in the field and control the timing of project development and capital expenditures;

Conduct field operations in an environmentally prudent manner;

Rigorously pursue opportunities to enhance production and recoveries from our existing pools;

Gain control of facilities and infrastructure where possible to reduce operating costs and maximize production;

Expand the production and prospect base through strategic acquisitions, land sales and farm-ins.

Conducting ourselves with integrity in business holds the entire company to a high standard in dealing with employees, industry partners, shareholders and other stakeholders. Our integrity does not rely on laws, regulations and standards, it comes from the character of our people and must be modeled starting at the top. To us, it means being honest and forthright, dealing with others fairly, and consistently making our best effort. Acting with integrity is a cornerstone of leadership. We believe strong leadership will foster a positive working environment for our employees, create trust with our shareholders, business associates and regulatory authorities and will result in more business opportunities for us.

OUR STRATEGY IN ACTION

We are very pleased with our progress in C1's inaugural year. We have made some important strides by following our strategy.

Solidified our team;

Grew our reserves by almost 400%;

Doubled our exit production rate compared to a year ago;

Implemented a waterflood on the "G" Pool at Gift Lake;

Added a new, high working interest, core area in Blueberry;

Closed the strategic corporate acquisition of Extreme Energy Corp.;

Enhanced our undeveloped land and prospect inventory;

Raised $10.0 million of equity capital.

Our fourth quarter 2004 production grew by 105% to 516 boe/d when compared to the 2003 exit production rate of 252 boe/d and was 10% higher than this year's third quarter. As the waterflood at Gift Lake was not initiated until December, incremental oil production from the "G" Pool was not significant in 2004. We anticipate that it will have a significant impact on production and cash flow in 2005 after we receive Good Production Practice ("GPP") status on the pool.

For the year ended December 31, 2004 our production averaged 501 boe/d, with cash flow from operations of $4.0 million and net income of $3.0 million. We drilled a total of five wells in the year with an 80% success rate. We also concluded the acquisition of Extreme Energy Corp. ("Extreme") in December 2004, which solidified our working interest in Blueberry. For the quarter there were net capital expenditures of $13.6 million, consisting of $2.7 million of exploration and development activities and $10.9 million in acquisition costs.

Our proved plus probable reserves grew substantially ending the year at 2.6 million boes, a 399% increase from last year. The reserve additions resulted primarily from reserve additions at Gift Lake, Chipmunk and the Extreme acquisition.

We believe that conducting our operations in an environmentally prudent manner is consistent with our corporate responsibility for environmental stewardship, but it is also an integral component in creating business opportunities. Our staff brings to C1 not only the experience of previous operations in major oil fields within sensitive areas, but also operations in unique oil and gas areas requiring dedicated commitments to working with governmental, non-governmental, First Nations and aboriginal communities. C1's commitment to integrity in business and operations provides a competitive advantage in accessing these new opportunities. C1 will continue to bring a consistently high level of commitment to our operations. We believe that it has reinforced and enhanced our ongoing relationship with the Gift Lake Métis, and will assist us in building new relationships with the Tsuu T'ina First Nation and other aboriginal groups as well as with industry partners.

C1 was fortunate to begin its existence with a rich endowment of undeveloped land. However, a key to our ongoing success is to unlock the value in those lands and continuously expand our land and prospect inventory. We rely on rigorous geological, geophysical and engineering analysis to generate further prospects. This has proven to be successful and we now have a drilling inventory of over 60 drill-ready prospects and have increased our undeveloped land and opportunity base to over 136,000 net acres. We will continue to focus on developing another new core area over the next year either through acquisition or farm-in arrangements so that we will remain in a position to high grade our drilling portfolio.

SUMMARY OF OPERATIONS AND FINANCIAL HIGHLIGHTS

	Three Months Ended December 31, 2004		Year Ended December 31, 2004	
Production				
Natural gas (mcf/d)		1,292		**1,017**
Oil and liquids (bbls/d)		306		**332**
Boe/d (6:1)		516		**501**
Financial ($000s except per unit amounts)	$	$/boe	$	$/boe
Oil and gas production	2,301	48.47	**8,718**	**47.51**
Royalties (net of ARTC)	(490)	(10.32)	**(2,033)**	**(11.08)**
Production expenses	(525)	(11.06)	**(1,693)**	**(9.22)**
Transportation	12	0.25	**(201)**	**(1.10)**
Operating netback	1,298	27.34	**4,791**	**26.11**
General and administrative	(214)	(4.51)	**(832)**	**(4.54)**
Current tax recovery	40	0.84	**–**	**–**
Cash flow from operations	1,124	23.67	**3,959**	**21.57**
Depletion and depreciation	(652)	(13.73)	**(4,531)**	**(24.69)**
Stock-based compensation	(194)	(4.09)	**(685)**	**(3.73)**
Future tax recovery	1,361	28.67	**4,248**	**23.15**
Net income (loss)	1,639	34.52	**2,991**	**16.30**
Earnings (loss) per share	$ 0.08		**$ 0.15**	

RESULTS OF OPERATIONS

Oil and Gas Production

($000s)	Three Months Ended December 31, 2004	Year Ended December 31, 2004
Crude oil sales	1,560	**6,278**
Natural gas sales	741	**2,440**
Total petroleum and natural gas sales	2,301	**8,718**

The primary reason for increased revenue in the fourth quarter compared the third quarter was due to higher production volumes combined with higher crude oil prices. Production volumes increased primarily in the Chipmunk area where we were able to increase production from the 06-22 well due to better than expected reservoir performance and in Seal where we restored shut-in production and made facilities modifications that significantly reduced battery down time.

Average Selling Prices

	Three Months Ended December 31, 2004	Year Ended December 31, 2004
Crude oil ($/bbl)	56.52	**51.78**
Natural gas ($/mcf)	6.30	**6.55**
Total average realized price ($/boe)	48.47	**47.51**

Crude Oil Pricing

C1 received an average price of $51.78/bbl for its crude oil for the year and $56.52 for the quarter ended December 31. Crude oil prices were 5% higher than the third quarter average price of $53.93/bbl. West Texas Intermediate (WTI) prices have remained strong throughout 2004, averaging more than US $41.50/bbl. Prices have been influenced by continued growth in oil demand, particularly from China and India as well as from uncertainty in the Middle East. Oil and gas markets have moved to "just in time" supply and demand which has resulted in little surplus capacity in the system for supply and has led to new bottoms for oil and gas prices at higher levels than in the past. Pricing is expected to remain strong for 2005 primarily due to continued demand growth with WTI prices expected to average US $43.00/bbl.

Natural Gas Pricing

C1 received an average price of $6.55/mcf for its natural gas production for the year and $6.30/mcf for the quarter ended December 31. Natural gas prices were down 4% compared to the third quarter average price of $6.56/mcf. C1 is currently marketing 100% of its gas to a third party based on the daily index price at AECO. Natural gas prices at AECO have averaged over $6.50/mcf in 2004 due to strong draws from storage in North America and the strength of crude oil prices. Due to expected higher gas storage levels, we anticipate that there will be some softness in natural gas prices in 2005 compared to last year, but should still average over $6.00/mcf at AECO.

Royalties

Royalty costs net of ARTC were $0.5 million for the fourth quarter ($10.32/boe). For the year royalty costs were $2.0 million ($11.08/boe) and the rates are expected to be similar for 2005 as Extreme's assets had a similar royalty burden to ours. Royalty costs per boe decreased from the third quarter amount of $11.70/boe due to a royalty holiday that was received on a well in the Seal area. Royalty burdens for C1 are predominantly crown. For the year, crown royalties before ARTC averaged 21.0% and freehold and other royalties averaged 4.9% of total revenue.

Production Expenses

Production expenses for the fourth quarter were $0.5 million ($11.06/boe) and were $1.7 million ($9.22/boe) year-to-date. This is higher than the third quarter cost of $8.57/boe primarily due to workover costs and battery repair and maintenance incurred at Seal during November. Production costs per boe in the Gift Lake, Seal and Milligan areas are currently high due to a low production base but costs in the Gift Lake area should begin to decline significantly after the first quarter of 2005 as we have obtained good production status ("GPP") and we will be able to increase production volumes at the "G" Pool. We also expect somewhat higher volumes in Seal as a result of a correction in emulsion measurement, which should reduce costs in that area on a boe basis.

Transportation Costs

Transportation costs for the year were $0.2 million ($1.10/boe). There was a small recovery overall for the fourth quarter resulting from over accruals in previous payments.

General and Administrative Expenses

General and administrative expenses were $0.2 million for the fourth quarter ($4.51/boe) down from last quarter and are $0.8 million ($4.54/boe) for the year. Administrative expenses were lower than in the third quarter primarily due to higher capital recoveries and an increase in capitalized general and administrative costs resulting from exploration and production staffing additions in the fourth quarter. Administrative costs per boe should decline as production volumes increase in 2005.

EXECUTE CORPORATE DEALS

C1 closed the acquisition of Extreme Energy Corp. in December 2004. The acquisition adds a new core area to C1's asset base and balances our asset mix at 50% oil and 50% gas. The acquisition contributes an estimated 220 boe/d light oil and natural gas production and doubled our total proved plus probable reserves at the close of the transaction.

Stock-based Compensation

Stock-based compensation for the fourth quarter was $10,000 higher than the third quarter due to additional options granted. The total compensation of $685,000 year-to-date represents a non-cash charge resulting from applying the fair value method on performance shares that were issued in 2003 and stock options issued in 2004. Under this method, compensation expense related to these programs is recorded in the statement of operation over the vesting period.

Depletion, Depreciation and Accretion

Depletion, depreciation, and accretion amounted to $0.7 million ($13.75/boe) in the fourth quarter and $4.5 million ($24.69/boe) for the nine-month period. The most important factor that impacted the depletion rate in the fourth quarter relates to the recognition of significantly higher reserves from the waterflood project at Gift Lake. We also obtained higher reservoir assessments resulting from better production performance in the Chipmunk area than was forecast as well as the effect of long reserve life assets acquired in the Extreme transaction.

Ceiling Test

C1 has applied a ceiling test on the carrying costs of petroleum and natural gas properties. The net amount at which petroleum and natural gas properties are carried is limited to the fair value of those properties based on the net present value of the future net revenues (the "ceiling test"). Commodity prices used to determine the future cash flows of C1 were taken from pricing forecasts published by C1's independent engineers and are consistent with forecast prices. The prices used for "light, sweet crude oil at Edmonton" are $51.25/bbl in 2005 reducing to $36.91 by 2010 and increasing at 1.5% per annum thereafter. Natural gas prices at AECO-C are $6.97/mcf in 2005, declining to $5.37/mcf by 2009 before increasing to $5.98/mcf by 2015 at which time prices increase at 1.5% per annum thereafter. The ceiling test resulted in no write-down.

Capital and Income Taxes

There were $4.2 million of future tax benefits recorded during the year. This resulted from recognizing future tax benefits due to the renunciation of $7.3 million of resource expenditures to flow through shareholders as well as from recognizing the value of future tax benefits not previously recorded due to uncertainty of utilization. As the reserve and production base have grown, that uncertainty was diminished.

At the end of 2004, we had $38.8 million of tax pools available for deduction against future taxable income. The tax pools available were as follows:

December 31 ($000s)	2004	2003
Canadian oil gas property expense	$ 12,672	$ 10,429
Canadian development expense	9,163	6,203
Canadian exploration expense	8,863	8,612
Foreign exploration and development expense	228	–
Undepreciated capital cost	5,529	2,636
Non-capital losses carried forward	624	5
Share issue costs	1,714	407
Total tax pools	$ 38,793	$ 28,292

Cash Flow from Operations and Net Income

Cash flow from operations was $1.1 million for the fourth quarter, a 19% increase from the third quarter, and $3.9 million for the year.

Net income was $2.9 million for the year ($0.15/share) with income for the fourth quarter of $1.6 million ($0.08/share).

Capital Expenditures

($000s)	Three Months Ended December 31, 2004	Year Ended December 31, 2004
Drilling and completions	$ 806	$ 8,292
Land	667	1,310
Equipment and facilities	979	3,021
Geological and geophysical	29	1,366
Asset retirement obligations	(104)	(57)
Capitalized general and administrative expenses	210	506
Property acquisitions	–	605
Corporate acquisition	10, 879	10,879
Other	167	171
Total capital expenditures	$ 13,633	$ 26,093

Capital expenditures for the year ended December 31, 2004 were 26.1 million. During the fourth quarter we incurred $2.8 million of exploration and development expenditures. These costs were primarily related to costs incurred in Gift Lake related to the waterflood, some drilling costs in Blueberry subsequent to the Extreme acquisition, and preliminary costs relating to the winter drilling program in Haro.

On December 16, 2004, C1 completed the acquisition of Extreme for $10.9 million (including costs associated with the acquisition of $0.2 million). Extreme shareholders received a total of 5,854,992 C1 common shares and 371,116 C1 share purchase warrants with an ascribed value of $0.1 million. Extreme was amalgamated with C1 on December 16, 2004. The assets acquired by C1 added production of approximately 220 boe/d (77% natural gas) to our existing production. In addition, the acquisition added approximately 20,000 net acres of undeveloped land and $8.0 million in tax pools and consolidated our working interest position in the Blueberry area. The transaction has been accounted for as a purchase and the financial statements of C1 include the results of the Extreme assets effective December 17, 2004.

Finding and Development Costs ("F&D") by Major Capital Type

	2004 Capital Expenditures	Change in Future Development Capital	Total Capital	Reserves Additions	Traditional F&D[1] ($/boe)	NI 51-01 F&D[2] ($/boe)
Proved reserves						
Exploration and development	**14,609**	2,240	17,034	938	15.57	17.96
Corporate acquisitions	**10,879**	350	11,229	491	22.16	22.87
Property acquisitions	**605**	450	1,055	19	31.84	55.53
Total	**26,093**	**3,040**	**29,133**	**1,448**	**18.02**	**20.12**
Proved plus probable reserves						
Exploration and development	**14,609**	4,809	19,418	1,354	10.79	14.34
Corporate acquisitions	**10,879**	788	11,667	851	12.78	13.78
Property acquisitions	**605**	850	1,455	94	6.44	14.82
Total	26,093	**6,447**	**32,540**	**2,299**	**11.35**	**14.15**
Recycle ratios[3]						
Total proved					1.20	1.07
Total proved plus probable					1.90	1.52

[1] Calculated excluding changes in future development capital.

[2] Calculated as outlined in NI 51-101, including the change in future development capital from the prior year end reserve report.

[3] Year ended December 31, 2004 cash flow from operations per share of $21.30 divided by total finding and development costs based on 2004 capital.

LIQUIDITY AND CAPITAL RESOURCES

Capital Resources

The Company uses various sources of capital to fund its capital program. The 2004 capital program was funded as follows:

($000s)	
Cash flow from operations	$ 3,959
Changes in working capital	194
Cash utilized	3,030
Increase in asset retirement obligations	(57)
Equity issued (net of issuance costs)	18,967
Total capital resources	$ 26,093

Funding of Capital Program

The 2005 capital program is currently budgeted at $17.0 million. C1 expects the majority of the capital expenditures to be funded by cash on hand, cash flow from operations and a small portion of bank debt.

Cash flow from operations is partially influenced by factors that the Company cannot control such as commodity prices, the US/Canadian dollar exchange rates and interest rates. C1's 2005 sensitivity to moderate fluctuations in key business parameters is shown in the accompanying table.

	Change in 2005 Cash Flow $000s	$/Share
Change of $1.00 US/bbl in the price of WTI oil	218	0.01
Change in oil production of 100 bbl/d	1,009	0.02
Change of $0.10 US/mcf in the price of NYMEX natural gas	202	0.01
Change in natural gas production of one mmcf/d	1,247	0.02
Change of 1% in the $US/$Cdn exchange rate	214	0.01

Working Capital

C1 had working capital of $4.4 million at December 31, 2004. This represents a decrease of $4.4 million from last quarter and a decrease of $4.6 million from last year. The primary reasons for the decline in working capital from the third quarter are due to the working capital deficiency assumed on the Extreme acquisition as well as from the increase in capital expenditures leading into the winter drilling program.

C1 expects that there will be significant fluctuations in working capital during the coming year. Two significant factors affecting working capital are capital expenditures and cash flow. Capital spending is expected increase significantly in the first quarter of 2005 as we have an active drilling program planned. Cash flow is also expected to fluctuate, as it is dependent on changes in items such as production volumes, commodity prices, operating costs, etc.

Bank Facilities

C1 has $8.5 million of credit facilities available with a Canadian chartered bank. The facilities are composed of a $7.0 million revolving demand loan plus a $1.5 million non-revolving acquisition/development demand loan. The interest rate on outstanding debt is set at the bank's prime lending rate plus 0.5% and 1.0%, respectively. The facilities are secured by a floating charge over all of C1's assets. No amount was outstanding at December 31, 2004.

We anticipate utilizing a portion of our credit facilities beginning in the first quarter of 2005 to equip and tie-in some new wells. However, we will monitor our debt levels carefully and do not expect it to exceed $5.0 million based on our 2005 budgeted capital expenditures of $17.0 million.

Share Capital

At December 31, 2004, C1 had 27,609,408 shares issued and outstanding with a weighted average number of shares outstanding of 20,475,249 (diluted - 21,332,027). Common shares outstanding at December 31, 2003 were 17,754,416 (diluted - 17,754,416).

During May 2004, we completed one flow-through common share issuance of 4,000,000 shares at a price of $2.50 per share for gross proceeds of $10.0 million.

On December 16, 2004 C1 issued 5,584,992 common shares and 371,116 share purchase warrants for all of the issued and outstanding shares and warrants of Extreme. C1 shares were valued at $1.80 per share.

C1 began trading on January 4, 2004 and during the year, 14.3 million C1 shares traded on The Toronto Stock Exchange with a high of $2.45 per share, a low of $1.50 per share and a close of $1.75 per share. C1's market capitalization at year end 2004 was approximately $48.3 million.

Contractual Obligations

($000s)	**Total**	2005	2006	2007	Thereafter
Office lease obligations	**396**	235	107	54	-
Operating lease obligation	**57**	57	-	-	-
Joint venture obligations	**1,500**	1,500	-	-	-
Flow through share obligations	**9,900**	9,900	-	-	-
	11,853	11,692	107	54	-

SELECTED ANNUAL AND QUARTERLY INFORMATION

($000s, except per share amounts)	Q1	Q2	Q3	Q4	Year	Three Day Period Ended December 31, 2003
Gross revenues before royalties	1,572	2,721	2,124	2,301	**8,718**	30
Cash flow from operations	798	1,133	904	1,124	**3,959**	(9)
Per share – basic and diluted ($)	0.04	0.06	0.04	0.05	**0.19**	0.00
Net income	2,565	(601)	(612)	1,639	**2,991**	(43)
Per share – basic ($)	0.14	(0.03)	(0.04)	0.07	**0.15**	0.00
Total assets	31,538	35,717	33,699	52,685	**52,685**	26,299

CRITICAL ACCOUNTING POLICIES

The preparation of the consolidated financial statements in accordance with Canadian GAAP requires management to make judgments and estimates that affect the financial results of the Company. The critical estimates are discussed below.

Full Cost Accounting

C1 follows the full cost method of accounting for petroleum and natural gas operations as outlined in Canadian Institute of Chartered Accountants ("CICA") accounting guideline "Oil and Gas Accounting – Full Cost" (AcG-16). Under this accounting method, all costs related to the exploration and development of petroleum and natural gas reserves are capitalized. Capitalized costs, as well as the estimated future expenditures to develop proved reserves, are depleted using the unit of production method based on estimated proved petroleum and natural gas reserves. The carrying value of petroleum and natural gas properties is limited to their fair value. The fair value is equal to estimated future cash flows from proved and probable reserves using future price forecasts and costs discounted at a risk-free rate.

Petroleum and Natural Gas Reserves

All of C1's petroleum and natural gas reserves are evaluated and reported on by independent petroleum engineering consultants. The estimation of reserves is a subjective process. Forecasts are based on engineering data, projected future rates of production, and the timing of future expenditures, all of which are subject to numerous uncertainties and various interpretations. The Company expects that its estimates of reserves will change to reflect updated information. Reserve estimates are critical to the following accounting estimates:

- Calculation of unit-of-production depletion and future site restoration rates. Proved reserve estimates are used to determine the DD&A rate applied to each unit of production.
- Ceiling test calculation, measurement of impairment of oil and gas assets. The fair value of future cash flows is estimated from proved and probable reserves using future price forecasts.

The above accounting estimates are critical to the determination of net earnings. These estimates, including the calculation of proved reserves, are affected by the following events:

- Changes to commodity prices;
- Production performance of wells;
- Changes to reservoir performance/pressures;
- New geological and geophysical data;
- Competitor production practices;
- Changes to government regulations.

Reserve estimates can be revised upward or downward based on the results of future drilling, testing or production levels.

RISK AND UNCERTAINTY

As an exploration and production company in the oil and gas industry, C1 is exposed to a number of business risks, which are beyond the control of management. These risks can be categorized as operational, financial and regulatory.

Operational risks include exploring for and developing oil and natural gas reserves on an economic basis, drilling risks, reservoir performance, access to contract services, availability of skilled labor and weather conditions affecting the timing of capital program completion. C1 maintains an insurance policy consistent with industry standards to protect against well blowouts and other drilling problems, destruction and damage to tangible assets, pollution and third-party liability coverage. In addition, we employ highly qualified staff and experienced contract services and provide a compensation environment that rewards above average performance, develops long-term relationships and provides measurement objectives consistent with shareholder value enhancement. Managing reservoir risk for a company our size is difficult due to the high asset concentration that currently exists with our assets. C1 is focused on diversification of our assets to provide a geologically diverse prospect inventory while protecting access to pipeline and facilities.

Financial risks include fluctuations in commodity price, interest rates and the Canadian/US dollar exchange rate. C1 does not have any hedge instruments in place to cover any of these named risks. As the production base begins to diversify, we will develop a hedging/risk management policy that will define strict controls to managing financial market exposure. Our approach to managing these risks is to maintain a healthy balance sheet with prudent levels of debt measured by debt to cash flow and debt coverage ratios. This allows for strong financial capacity to maintain exploration and development activities in any downturn in commodity prices. An additional financial risk is credit risk for failure of performance by counter-parties. This risk is controlled by an evaluation of the credit risk before contract initiation and ensuring product sales and delivery contracts are made with well-known and financially strong crude oil and natural gas marketers.

The oil and gas industry is a heavily regulated industry with respect to environmental and safety practices. However, production and drilling practices of competitors may challenge the regulations creating production disruptions for the Company. With respect to environmental and safety issues, we maintain an environmental and safety policy with a well-defined reporting process to the Board of Directors. Other regulatory risks include changes to royalty and tax legislation over which the Company has no control.

Additional information relating to the Company can be found on Sedar at **www.sedar.com**.

MANAGEMENT'S REPORT

To the Shareholders of C1 Energy Ltd.

The preparation and presentation of the Company's financial statements is the responsibility of management. The financial statements have been prepared in accordance with generally accepted accounting principles (GAAP) and include management's best estimates and judgments, where required. The financial information contained elsewhere in this annual report is consistent with the financial statements.

Management is responsible for installing and maintaining a system of internal controls to provide reasonable assurance that assets are safeguarded and that reliable financial information is produced for preparation of the financial statements.

The Board of Directors is responsible for ensuring management's performance of its responsibilities for financial reporting and internal control. The Board exercises this responsibility with the assistance of the Audit Committee. The Audit Committee meets with management and the independent auditors to satisfy itself that management's responsibilities are properly discharged, to review the consolidated financial statements and recommend that the financial statements be presented to the Board of Directors for approval.

Deloitte & Touche LLP, the independent auditors, are appointed by the shareholders to express an opinion as to whether the financial statements present fairly the Company's financial position, results of operations and cash flows in accordance with GAAP. The external auditors have full and unrestricted access to the Audit Committee to discuss their audit and related findings.

Hugh Pattillo
President and Chief Executive Officer

Gary Lobb, CA
Vice President of Finance and Chief Financial Officer

Calgary, Alberta
March 11, 2005

AUDITORS' REPORT

To the Shareholders of C1 Energy Ltd.

We have audited the balance sheets of C1 Energy Ltd. as at December 31, 2004 and 2003 and the statements of operations and retained earnings and cash flows for the year ended December 31, 2004 and for the period from commencement of operations on December 29, 2003 to December 31, 2003. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2004 and 2003 and the results of its operations and its cash flows for the year ended December 31, 2004 and for the period from commencement of operations on December 29, 2003 to December 31, 2003 in accordance with Canadian generally accepted accounting principles.

Deloitte & Touche LLP

Chartered Accountants

Calgary, Alberta
March 11, 2005

BALANCE SHEETS

As at December 31 (dollars in thousands)

	2004	2003
ASSETS		
Current assets		
Cash and cash equivalents	$ 6,930	$ 9,960
Accounts receivable	3,754	32
Prepaid expenses	80	198
	10,764	10,190
Property and equipment (note 4)	34,158	16,109
Goodwill (note 3)	5,780	–
Future income tax asset (note 8)	1,983	–
	$ 52,685	$ 26,299
LIABILITIES		
Current liabilities		
Accounts payable and accrued liabilities	$ 6,296	$ 1,209
Asset retirement obligations (note 7)	536	368
	6,832	1,577
Commitments (note 11)		
SHAREHOLDERS' EQUITY		
Share capital (note 5)	42,072	27,768
Warrants (notes 3 and 5)	91	–
Contributed surplus (note 5)	699	14
Retained earnings (deficit)	2,991	(3,060)
	45,853	24,722
	$ 52,685	$ 26,299

See accompanying notes to the financial statements.

Approved by the Board,

Raymond Chan
Director

Hugh Pattillo
Director

STATEMENTS OF OPERATIONS AND RETAINED EARNINGS

For the year ended December 31, 2004 and the period from commencement of operations on December 29, 2003 to December 31, 2003
(dollars in thousands except per share amounts)

	Year Ended December 31, 2004	Three Day Period Ended December 31, 2003
Revenue		
Petroleum and natural gas sales	$ 8,718	$ 30
Royalties, net of Alberta Royalty Tax Credit	(2,033)	(5)
	6,685	25
Expenses		
Production	1,693	8
Transportation	201	–
General and administrative	832	26
Stock-based compensation (note 5)	685	14
Depletion, depreciation and accretion	4,531	20
	7,942	68
Loss before income taxes	(1,257)	(43)
Income taxes (note 8)	(4,248)	–
Net income (loss)	2,991	(43)
Retained earnings (deficit), beginning of period	(3,060)	–
Elimination of accumulated deficit (note 5)	3,060	–
Effect of changes in accounting policies (notes 1 and 4)	–	(3,017)
Retained earnings, end of period	$ 2,991	(3,060)
Net income (loss) per common share (note 6)		
– Basic	$ 0.15	$ 0.00
– Diluted	$ 0.14	$ 0.00

See accompanying notes to the financial statements.

STATEMENTS OF CASH FLOWS

For the year ended December 31, 2004 and the period from commencement of operations on December 29, 2003 to December 31, 2003
(dollars in thousands)

	Year Ended December 31, 2004	Three Day Period Ended December 31, 2003
Cash provided by (used in)		
Operating activities		
Net income (loss)	$ 2,991	$ (43)
Add (deduct):		
Future income tax recovery	(4,248)	–
Depletion, depreciation and accretion	4,531	20
Stock-based compensation	685	14
Funds from operations	3,959	(9)
Net change in non-cash working capital (note 10)	910	672
	4,869	663
Investing activities		
Property and equipment expenditures	(15,272)	(557)
Cash paid on Extreme acquisition (note 3)	(1,272)	–
Net change in non-cash working capital (note 10)	(716)	307
	(17,260)	(250)
Financing activities		
Issuance of common shares	10,000	9,960
Share issue costs	(639)	(413)
	9,361	9,547
Net increase (decrease) in cash and cash equivalents	(3,030)	9,960
Cash and cash equivalents, beginning of period	9,960	-
Cash and cash equivalents, end of period	$ 6,930	$ 9,960

See accompanying notes to the financial statements.

For the year ended December 31, 2004 and the period from commencement of operations on December 29, 2003 to December 31, 2003
(tabular dollar amounts in thousands except per share or unit amounts)

1. SIGNIFICANT ACCOUNTING POLICIES

Business and basis of presentation

C1 Energy Ltd. ("C1" or the "Company") is a Calgary-based oil and natural gas exploration and production company whose key business activities are focused in Alberta. The Company was incorporated on September 25, 2003 and commenced operations on December 29, 2003 when a portion of the assets of Navigo Energy Inc. ("Navigo") were transferred to C1 under a Plan of Arrangement (note 2). C1 is a public company and commenced trading on the Toronto Stock Exchange on January 6, 2004 under the symbol "CTT".

These financial statements are prepared in accordance with accounting principles generally accepted in Canada. Management has made the necessary estimates and assumptions regarding certain types of assets, liabilities, revenues and expenses in the preparation of the financial statements. Actual results could differ from those estimates. Significant accounting policies are summarized as follows:

a) Cash and cash equivalents

Cash and cash equivalents consists of cash in the bank, less outstanding cheques, and deposits with a maturity of less than three months at the time of purchase.

b) Petroleum and natural gas properties

i) Full cost accounting

The Company uses the full cost method of oil and gas accounting whereby all costs relating to the exploration for and development of petroleum and natural gas reserves are capitalized. Such costs include land acquisition, drilling of productive and non-productive wells, geological and geophysical, production facilities, carrying costs directly related to unproved properties and corporate expenses directly related to acquisition, exploration and development activities. Gains or losses on sales of properties are recognized only when crediting the proceeds to costs would result in a change of 20% or more in the depletion rate.

ii) Depletion and depreciation

Depletion of exploration and development costs and depreciation of production equipment is provided using the unit-of-production method based upon estimated gross proved petroleum and natural gas reserves. For purposes of this calculation, petroleum and natural gas reserves are converted to a common unit of measurement on the basis of six thousand cubic feet of gas equating to one barrel of oil equivalent (boe). The costs of significant undeveloped properties are excluded from costs subject to depletion. Unproved properties are evaluated for impairment on an annual basis.

iii) Ceiling test

The net amount at which petroleum and natural gas properties are carried is limited to the fair value of those properties based on the net present value of the estimated future net revenues (the "ceiling test"). This a two-stage process which is to be performed at least annually. The first stage is a recognition test which compares the undiscounted future cash flow from proved reserves plus the cost less impairment of unproved properties to the net book value of the petroleum and natural gas assets to determine if the assets are impaired. An impairment loss exists when the carrying amount of the petroleum and natural gas assets exceeds such undiscounted cash flow. The amount of impairment, if any, to be recorded is

measured as the amount by which the carrying amount of assets capitalized exceeds the sum of: (i) the expected net present value of future net revenues from proved and probable reserves discounted at a risk free interest rate and (ii) the costs (less any impairment) of unproved properties that have been subject to a separate test for impairment. Commodity prices used to determine future net revenues are based on the best information available to the Company and are consistent with quoted benchmark prices in the futures market (adjusted for quality differences). If the net carrying costs exceed the fair value, the impairment is recorded as additional depletion and depreciation.

c) *Goodwill*

Goodwill is recorded at cost (less impairment, if any) and is not amortized. The Company must record goodwill relating to a corporate acquisition when the total purchase price exceeds the fair value for accounting purposes of the net identifiable assets and liabilities of the acquired company.

The goodwill balance is assessed for impairment annually at year-end or as events occur that could result in an impairment. Impairment is recognized based on the fair value of the reporting entity (the Company) compared to the book value of the reporting entity. If the fair value of the Company is less than the book value, impairment is measured by allocating the fair value of the Company to the identifiable assets and liabilities as if the Company had been acquired in a business combination for a purchase price equal to its fair value. The excess of the fair value of the Company over the amounts assigned to the identifiable assets and liabilities is the fair value of the goodwill. Any excess of the book value of goodwill over this implied fair value of goodwill is the impairment amount. Impairment is charged to earnings in the period in which it occurs.

d) *Asset retirement obligations*

The Company recognizes the fair value of the asset retirement obligations related to its property and equipment, using expected cash flows discounted at a credit-adjusted risk-free rate, for future asset retirement costs in the period in which they are incurred. Upon initial recognition of a liability for future asset retirement costs, the carrying value of the petroleum and natural gas properties is increased by the amount of the liability. These costs are included in the carrying value subject to depletion and depreciation and the ceiling test. The liability accretes until the expected settlement date. Subsequent changes to the fair value of the liability arising from revisions to the timing or amount of the original estimate of undiscounted cash flows are recognized as an increase or a decrease in the carrying amount of the obligation and are capitalized as part of the carrying value of the petroleum and natural gas properties. Retained earnings increased by $209,000 upon adoption of the new accounting standard on December 29, 2003 as this policy differed from Navigo's accounting policy at the date of transfer (note 2).

e) *Foreign currency*

Monetary assets and liabilities denominated in foreign currencies are translated into Canadian dollars at year-end exchange rates. Non-monetary items are translated at the average exchange rate during the month they are recognized. Exchange gains or losses are included in income in the period incurred.

f) *Measurement uncertainty*

The amounts recorded for depletion, depreciation and accretion are based on estimates of reserves and future costs as well as estimates of reserves in the case of depletion and depreciation. By their nature, these estimates and those related to the assessment of estimated future cash flows used to assess impairment, are subject to measurement uncertainty and the impact on the financial statements of future periods could be material.

g) *Joint interests*

A portion of the Company's exploration, development and production activities are conducted jointly with others. These financial statements reflect only the Company's proportionate interest in such activities.

h) Revenue recognition

Revenue associated with sales of crude oil, natural gas, and natural gas liquids is recognized when title passes to the purchaser, normally at the pipeline delivery point for natural gas and at the wellhead for crude oil.

i) Flow-through shares

The Company has financed a portion of its exploration and development activities through the issue of flow-through shares. Under the terms of the flow-through share agreements, the tax attributes of the related expenditures are renounced to the subscribers. Share capital is reduced and future income tax liability is increased by the estimated cost of the renounced tax deductions at the time the expenditures are renounced.

j) Hedging

The Company may periodically utilize certain financial instruments to reduce exposures related to petroleum and natural gas prices and foreign exchange fluctuations on a portion of its crude oil and natural gas production in accordance with Company policy. Under hedge accounting, gains and losses on these contracts, all of which must constitute effective hedges, are recognized in revenue concurrently with the hedged transaction. If hedge requirements are not met, the financial instruments are recorded at fair value; any gains or losses are included in income in the period.

k) Future income taxes

The Company follows the liability method of accounting for income taxes. Under this method future tax assets and liabilities are determined based on differences between the financial reporting and tax bases of assets and liabilities and measured using the substantively enacted tax rates and laws that will be in effect when the differences are expected to reverse.

l) Stock-based compensation

The Company has stock-based compensation plans, which are described in note 5. Compensation expense is recognized for these plans when stock options or performance shares are issued to employees. Any consideration paid by employees upon exercise of stock options is credited to share capital. Compensation costs are recognized in the statement of operations and included in contributed surplus.

m) Per share amounts

Net income per share is calculated using the weighted average number of shares outstanding during the period. Diluted net income per share is calculated using the treasury stock method to determine the dilutive effect of stock options and other dilutive elements. The treasury method assumes that the proceeds received from the exercise of "in the money" stock options are used to re-purchase and cancel common shares at the average trading price for the period.

2. PLAN OF ARRANGEMENT

On December 29, 2003, as a result of a Plan of Arrangement (the "Arrangement") between Navigo and C1 certain oil and gas properties were transferred to C1. In exchange, the former Navigo shareholders received one share of C1 for every three shares they held prior to the Arrangement. The number of shares of C1, which were issued to former Navigo shareholders as a result of this transaction, was 12,192,698. At the time of the transaction, C1 and Navigo were related companies resulting in the transfer of assets and related liabilities to C1 from Navigo at their carrying value.

Net assets transferred:	
Petroleum and natural gas properties	$ 18,430
Future removal and site restoration	(352)
Consideration – shares issued at net book value	$ 18,078

3. CORPORATE ACQUISITION

On December 16, 2004, C1 acquired Extreme Energy Corp. ("Extreme") and Extreme shareholders received 0.22 of a common share of C1 ("C1 Common Share") for each common share of Extreme (5,854,992 C1 Common Shares at an ascribed value of $1.80 per common share). The total cost to C1 to acquire the Extreme shares was $10,878,719 including transaction costs of $248,633 and 371,116 warrants at an ascribed value of $91,100. This transaction has been accounted for using the purchase method with the results of Extreme being included in the statement of operations of C1 from December 17, 2004.

The following table summarizes the allocation of the purchase price to the estimated fair value of the assets acquired and liabilities assumed as at the closing date.

Bank indebtedness	$ (1,023)
Accounts receivable	1,641
Prepaid expenses and deposits	38
Petroleum and natural gas properties	7,347
Goodwill	5,780
Accounts payable and accrued liabilities	(2,970)
Future income tax asset	273
Asset retirement obligations	(207)
	$ 10,879

4. PROPERTY AND EQUIPMENT

	2004	2003
Petroleum and natural gas properties and equipment	**$ 41,917**	$ 19,355
Accumulated depletion and depreciation	**(7,759)**	(3,246)
Net book value	**$ 34,158**	$ 16,109

At December 31, 2004, $16.7 million (2003 – $10.6 million) of costs relating to unproved properties, and seismic were excluded from costs subject to depletion.

During 2004, $506,000 (2003 – $nil) of general and administrative expenses relating to exploration and development activities were capitalized.

The ceiling test in 2004 was calculated using the following prices:

	Light, Sweet Crude Oil at Edmonton	AECO-C Spot	Exchange Rate ($US/$Cdn)
2005	51.25	6.97	0.84
2006	48.03	6.66	0.84
2007	42.64	6.21	0.84
2008	38.31	5.73	0.84
2009	36.36	5.37	0.84
2010 onwards	Prices increase at 1.5% per year		Constant at 0.84

There was no impairment in 2004. An impairment of $3.2 million resulted from the ceiling test in 2003. The charge was made to retained earnings as a result of the adoption of the new accounting guideline as described in note 1(b) which differed from that of Navigo at the time of the transfer of assets (note 2).

5. SHARE CAPITAL

a) Authorized

The Company is authorized to issue an unlimited number of common shares and 1,442,000 performance shares.

b) Issued and outstanding

Common Shares	Number of Shares	Amount
Balance, December 29, 2003	–	$ –
Flow-through shares issued (i)	2,066,670	3,100
Flow-through shares issued (ii)	119,048	200
Common shares issued (iii)	1,476,000	2,657
Flow-through shares issued (iii)	1,900,000	3,990
Share issue costs, net of tax (iii)		(270)
Common shares issued on Plan of Arrangement (iv)	12,192,698	18,078
Balance at December 31, 2003	17,754,416	27,755
Flow-through shares issued (v)	4,000,000	10,000
Tax effect of renunciation of resource expenditures on flow-through shares (vi)	–	(2,886)
Issued on Extreme acquisition (note 3)	5,854,992	10,637
Share issue costs, net of future tax benefit of $251,452 (v)	–	(387)
Reduction in stated capital (vii)	–	(3,060)
Balance at December 31, 2004	**27,609,408**	**$ 42,059**

i) On December 23, 2003 C1 completed an initial private placement of 6,200,000 Class B Non-voting Shares, at $0.50 per share, for aggregate proceeds of $3.1 million (2,066,670 C1 Common Shares ("C1 Common Shares") at $1.50 per share after giving effect to the Arrangement). The shares were issued on a flow-through basis and the tax effect of the renouncement was recorded in 2004, when the related expenditures were renounced.

ii) On December 23, 2003 the Company completed a private placement of 357,144 C1 Non-voting Shares issued on a flow-through basis at a price of $0.56 per share (119,048 C1 Common Shares at $1.68 per share after giving effect to the Arrangement) to a new officer of the Company for proceeds of $0.2 million. The tax effect of the renouncement was recorded in 2004, when the related expenditures were renounced.

iii) On December 29, 2003, C1 completed a brokered private placement pursuant to which the Company issued 5,700,000 C1 Energy Non-voting Shares on a flow-through basis at a price of $0.70 per share (1,900,000 C1 Common Shares at $2.10 per share after giving effect to the Arrangement) and 4,428,000 C1 Energy Non-Voting Shares at a price of $0.60 per share (1,476,000 C1 Common Shares at $1.80 per share after giving effect to the Arrangement). Aggregate proceeds were $6.2 million after deducting share issue costs of $0.4 million ($0.3 million after tax). The tax effect of the renouncement was recorded in 2004, when the related expenditures were renounced.

iv) The Arrangement was completed on December 29, 2003 and 12,192,698 C1 Common Shares were issued to former holders of Common Shares of Navigo.

v) On May 18, 2004 C1 completed a private placement equity financing to issue 4,000,000 C1 Common Shares on a flow-through basis at a price of $2.50 per share for total proceeds of $10,000,000 prior to share issuance costs of $0.4 million (net of future tax benefit of $0.3 million). The tax effect of the renouncement was recorded in 2004, when the related expenditures were renounced. In accordance with the terms of the C1 and Extreme's various flow-through share offerings, and pursuant to certain provisions of the Income Tax Act (Canada), the Company committed to renounce, for income tax purposes, exploration expenditures related to the purchases of its flow-through shares in the aggregate of $9,900,000 that had yet to be expended under these agreements.

vi) In accordance with the terms of the Company's various flow-through share offerings, and pursuant to certain provisions of the Income Tax Act (Canada), in 2004 the Company renounced, for income tax purposes, exploration expenditures related to the purchases of its flow-through shares in the aggregate of $7,290,000.

vii) Pursuant to a vote by the shareholders at the annual and special general meeting on March 18, 2004, C1's accumulated deficit at December 31, 2003 was eliminated by a reduction in stated capital.

Performance Shares	Number of Shares	Amount
Issued on December 23, 2003 (i)	1,344,000	$ 13
Balance at December 31, 2003 and 2004	**1,344,000**	**$ 13**

i) On December 23, 2003, C1 issued a total of 1,344,000 C1 Energy Performance Shares ("Performance Shares") at an issue price of $0.01 per share. Each Performance Share is convertible into the percentage of a C1 Common Share equal to the closing trading price of the C1 Common Shares on the Toronto Stock Exchange (the "Closing Price") less $1.35, if positive, divided by the Closing Price. Each Performance Share is convertible, at the option of the holder, into C1 Common Shares as to 1/3 on each of the day following the first, second and third anniversaries from the date of issuance. If the C1 Closing Price less $1.35 is not positive on any conversion date, C1 has the right, subject to applicable laws, to redeem the Performance Shares that would have otherwise been converted at the redemption price of $0.01 per share. The fair value of each Performance Share was determined, at date of issuance, using the Black-Scholes model with the variables described in note 5(c).

Warrants	Number of Warrants	Amount
Balance at December 31, 2003	–	$ –
Issued on Extreme acquisition (note 3)	371,116	91
Balance at December 31, 2004	**371,116**	**$ 91**

On the acquisition of Extreme, C1 issued 371,116 share purchase warrants to Extreme warrant holders with an ascribed price of $91,000 on the same pro rata terms as the Extreme common shareholders. The fair value of each warrant was determined, at the date of issuance, using the Black-Scholes model. The fair value of the warrants issued was estimated to be $0.24 per share using a risk free interest rate of 4.0%, volatility of 50%, and an average expected life of 0.6 years. This amount is amortized over the life of the warrant and is included in stock-based compensation expense. Additional details on the share purchase warrants outstanding at December 31, 2004 are as follows:

Exercise Price ($/share)	Number of Options (000s)	Contractual Life (years)	Expiry Date
2.25	55,500	0.67 years	August 31, 2005
2.48 (i)	272,514	0.57 years	July 27, 2005
2.70	43,602	0.57 years	July 27, 2005
2.47	371,116	0.58 years	

i) Each warrant entitles the holder to purchase one common share of the company at a price of $2.48 per share or one flow through common share at a price of $2.93 per share until expiry on July 27, 2005.

Contributed Surplus	Amount
Stock-based compensation	$ 14
Balance at December 31, 2003	14
Stock-based compensation	685
Balance at December 31, 2004	**$ 699**

c) Stock-based compensation

The fair value of each Performance Share was determined, at the date of issuance, using the Black-Scholes model. The fair value of the Performance Shares issued was estimated to be $0.78 per share using a risk free interest rate of 3.5%, volatility of 43%, and an expected life of three years. This amount is amortized over the life of the Performance Share and is included in stock-based compensation expense (2004 – $609,000; 2003 – $14,000).

C1 issued 625,000 options to purchase C1 Common Shares to certain officers and employees during the year. The options have a term of five years and vest over three years on the basis of one-third per year at exercise prices between $1.75-$1.95 per share. The fair value of each option was determined at the stock option grant date using the Black-Scholes model. The fair value was estimated to be an average of $0.72 per share using a risk free interest rate of 4.0%, average volatility of 47%, and an expected life of 3 years. This value is amortized over the life of the options and is included in stock-based compensation expense (2004 – $76,000; 2003 – $nil).

Additional details on the Company's stock options outstanding at December 31, 2004 are as follows:

Exercise Price ($/share)	Number of Options (000s)	Contractual Life (years)	Options Exercisable (000s)
1.91	175,000	4.46 years	–
1.95	125,000	4.50 years	–
1.75	325,000	4.88 years	–
1.83	625,000	4.64 years	–

6. EARNINGS PER SHARE

C1 uses the treasury stock method to determine dilution resulting from the issuance of stock options, warrants and other dilutive instruments. The number of shares used to calculate the diluted net income per share for the year ended December 31, 2004 included the weighted average number of C1 Common Shares outstanding of 20,475,249 plus 856,778 shares related to the dilutive effect of the conversion of performance shares and stock options. There was no effect for 2003 as the Company did not commence trading on the public markets until January, 2004. In calculating the weighted-average number of diluted C1 Common Shares outstanding for the year ended December 31, 2004, 371,116 share purchase warrants were excluded because their exercise price was greater than the average common share market price during the period the warrants were outstanding.

7. ASSET RETIREMENT OBLIGATIONS

The following table presents the reconciliation of the beginning and ending aggregate carrying amount of the obligation associated with the retirement of oil and gas properties:

	2004	2003
Asset retirement obligations, beginning of period	$ 368	$ –
Liabilities incurred	256	368
Accretion expense	18	–
Change in estimated future cash flows	(106)	–
Asset retirement obligations, end of period	$ 536	$ 368

At December 31, 2004, the total undiscounted asset retirement obligation is estimated to be $4.2 million. A 2% inflation rate and a 9% discount rate assumption have been used to estimate the obligations. Most of the obligations related to oil and natural gas wells are expected to be settled from 2020 to 2025 and those related to the facilities settled up to 2039 with all being funded from general resources at the time of settlement.

8. INCOME TAXES

The components of the future income tax asset are as follows:

	2004	2003
Future income tax assets		
Property and equipment	$ 1,314	$ 4,792
Share issue costs	620	166
Resource allowance	49	(154)
	1,983	4,804
Future tax benefits not recognized due to uncertainty of utilization	–	(4,804)
Net future income tax asset	$ 1,983	$ –

The provision for income taxes differs from the result that would be obtained by applying the combined Canadian Federal and Provincial statutory income tax rates to income before income taxes. This difference results from the following:

	2004	2003
Loss before taxes	$ (1,257)	$ (43)
Income tax rate	39.6%	40.7%
Expected income tax recovery	(498)	(18)
Increase (decrease) in taxes resulting from:		
Crown royalties (net of ARTC)	467	2
Resource allowance	(340)	–
Stock based compensation	271	5
Share issue costs	(87)	–
Future tax benefits (recognized) not recognized	(4,061)	11
Income tax recovery	$ (4,248)	$ –

The Company included a valuation allowance of $4,804 at December 31, 2003 due to the uncertainty at that time associated with being able to utilize the tax benefits in the future. That uncertainty was reduced in 2004 such that the future tax benefit was recognized.

The Company has the following tax deductions available to reduce future taxable income:

	2004	2003
Canadian oil and gas property expense	$ 12,672	$ 10,429
Canadian development expense	9,163	6,203
Canadian exploration expense	8,863	8,612
Foreign exploration and development expense	228	–
Undepreciated capital cost	5,529	2,636
Non-capital losses carried forward	624	5
Share issue costs	1,714	407
Total available tax pools	$ 38,793	$ 28,292

9. FINANCIAL INSTRUMENTS

The carrying value of the Company's cash and cash equivalents, accounts receivable, and accounts payable approximates their fair value due to the short term nature of these balances.

Substantially all of the Company's accounts receivable are due from customers in the oil and gas industry and are subject to the normal industry credit risks. The carrying value of accounts receivable reflects management's assessment of the associated credit risks.

The nature of the Company's operations results in exposure to fluctuations in commodity prices, exchange rates and interest rates. The Company, when appropriate, will utilize derivative contracts to manage its exposure to these risks.

10. SUPPLEMENTARY CASH FLOW INFORMATION

Changes in non-cash working capital items increased (decreased) cash and cash equivalents as follows:

	2004	2003
Accounts receivable	$ (3,723)	$ (32)
Prepaid expenses	119	(198)
Accounts payable and accrued liabilities	5,088	1,209
Non-cash working capital deficiency acquired	(1,290)	–
Change in non-cash working capital	$ 194	$ 979
Operating activities	$ 910	$ 672
Investing activities	(716)	307
Change in non-cash working capital	$ 194	$ 979

There were no amounts paid for interest expense or income and capital taxes during 2003 or 2004.

11. COMMITMENTS

In October 2004, C1 entered into a sublease agreement with a third party for office space. The sublease continues until March 2006. C1 pays approximately $170,000 per annum for rent and operating costs.

C1 has committed to incur $9.9 million in qualifying expenditures related to flow-through share arrangements by December 31, 2005.

The Company has entered into a farm-in agreement with Navigo Energy Inc. whereby C1 will equalize in a 32-section block and five cased wells in Haro for a 50% working interest by drilling five shallow gas wells prior to March 31, 2005. The Company had commitments with other third parties to drill a total of three wells during 2005 and one additional well in both 2006 and 2007 in separate farm-in agreements.

The Company has guarantees and other commitments in the normal course of business which, in the opinion of management, would not have a material adverse effect on the Company's liquidity, financial condition or results of operations.

In conjunction with the Plan of Arrangement, the Company entered into an administrative services agreement with Navigo. Navigo provides general administrative, accounting, marketing, land and information technology services to C1. In consideration for such services, C1 paid Navigo an administration fee of $287,000 in 2004 ($nil – 2003) based on the production of C1 divided by the combined production of C1 and Navigo. The Company paid the administration fees to Navigo until October, 2004. The companies continued to provide technical and administrative services to each other until February 2005 at which time the agreement was terminated.

	Year Ended December 31, 2004	Three Day Period Ended December 31, 2003
Financial ($000s, except share information)		
Petroleum and natural gas sales	**8,718**	30
Cash flow from operations[1]	**3,959**	(9)
Per share basic and diluted	**0.19**	0.00
Net income	**2,991**	(43)
Per share – basic	**0.15**	0.00
Per share – diluted	**0.14**	0.00
Capital expenditures, net	**26,093**	16,130
Working capital	**4,468**	8,981
Total assets	**52,685**	26,299
Shareholders' equity	**45,853**	24,722
Common shares outstanding (000s)	**27,609**	17,754
Weighted average common shares outstanding (000s)	**20,475**	17,754
Operations		
Crude oil and NGLs production		
Barrels	**121,466**	567
Barrels per day	**332**	189
Average selling price ($/bbl)	**51.78**	43.22
Natural gas production		
Thousand cubic feet	**372,245**	1,142
Thousand cubic feet per day	**1,017**	381
Average selling price ($/mcf)	**6.55**	4.85
Oil equivalent production		
Barrels of oil equivalent	**183,507**	757
Barrels of oil equivalent per day (6:1)	**501**	252
Average selling price ($/boe)	**47.51**	39.67
Average operating netback ($/boe)	**26.11**	23.25
Wells drilled		
Gross	**5**	–
Net	**3.7**	–

[1] The Company, in part, evaluates its performance based on cash flow from operations. Cash flow from operations is a non-GAAP measure that represents cash generated from operating activities before changes in non-cash working capital items during the period. Cash flow from operations may not be comparable to similar measures used by other companies.

Please note that all natural gas values are converted to a barrel of oil equivalent ("boe") on a 6:1 ratio unless otherwise stated. Boes may be misleading, particularly if used in isolation. A boe conversion ratio of 6 mcf:1 bbl is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead.

This report should be read in conjunction with previously released public documents. The comparative figures for 2003 include only three days of results of operations as C1 Energy Ltd. was established on December 29, 2003.

MANAGEMENT AND DIRECTORS

HUGH PATTILLO - PRESIDENT AND CHIEF EXECUTIVE OFFICER, DIRECTOR

Mr. Pattillo has over 20 years of management and technical experience in the oil and gas industry. Mr. Pattillo became President and Chief Executive Officer of C1 Energy in December 2003 after directing exploration for Navigo as its Vice President, Exploration from July 2002. Previously, Mr. Pattillo was Chief Geophysicist at Petromet Resources Ltd. and Chief Geophysicist and Northern Exploration Leader for Beau Canada Exploration Ltd. Mr. Pattillo graduated with Bachelor of Science (Honours Geophysics) from the University of Western Ontario in 1982.

GARY LOBB - VICE PRESIDENT OF FINANCE AND CHIEF FINANCIAL OFFICER, DIRECTOR

Mr. Lobb has over 20 years of financial experience, and became Vice President of Finance and Chief Financial Officer of C1 Energy in December 2003. Formerly Mr. Lobb was Vice President of Finance, Chief Financial Officer and Corporate Secretary of Nycan Energy Corp. from January 2002 to May 2003; and held the same role at Tetonka Drilling Inc. until the October 2000 merger of Tetonka Drilling Inc. and Bonus Well Services Corp. Prior to the merger, Mr. Lobb was the Chief Financial Officer of Tetonka Drilling Inc. since 1997. Mr. Lobb graduated with a Bachelor of Commerce degree from the University of Calgary in 1983.

RON BARMBY - VICE PRESIDENT AND CHIEF OPERATING OFFICER, DIRECTOR

Mr. Barmby P.Eng, M.Eng, has more than 20 years of operations experience. He joined C1 as the Vice President of Operations in September 2004 and was promoted to Vice President and Chief Operating Officer in early 2005. Previously, Mr. Barmby was Vice President, Production & Engineering of Navigo Energy Inc. between December 2001 and June 2004 and was Vice President of Gulfstream Resources from 1995 to 2001. Mr. Barmby also worked with Amerada Hess Canada as their Drilling & Completions Manager and Production Manager.

BILL VANDERVEEN - VICE PRESIDENT OF EXPLORATION, DIRECTOR

Mr. VanderVeen P.Geol., has 26 years of oil and gas exploration experience in the Western Canadian Sedimentary basin. Mr. VanderVeen joined C1 as Vice President Exploration in October 2004. Previously Mr. VanderVeen was with Navigo Energy from July 2002 and was a senior geologist at Encal from January 2001 to June 2002, and was a geological consultant for various small and medium sized exploration and development companies.

GARY CAMPBELL - LAND MANAGER

Mr. Campbell has 23 years of experience in the oil and gas industry. He began consulting to C1 in January 2004 and became Land Manager in June 2004. Prior to joining C1, Mr. Campbell was Team Lead - Business Development for Encana from September 2002 to December 2003. Previously he was a regional landman at Petro-Canada from January 1999 to September 2002, and Vice President of Land and Contracts at Brandon Energy from April 1996 to April 1998.

JIM DITTRICH - CHIEF GEOPHYSICIST

Mr. Dittrich has 23 years of experience in the Western Canadian Sedimentary basin exploring for oil and gas. Prior to joining C1 as a Senior Geophysicist in October 2004, Mr. Dittrich was Senior Geophysicist at Navigo Energy Inc. since 2002. In the last 10 years, Mr. Dittrich was a Chief Geophysicist at Magin Energy and Senior Geophysicist at Sceptre Resources and CNRL.

STACEY RADLEY - MANAGER, ENGINEERING

Mr. Radley is a professional engineer with 11 years of experience in the oil and gas industry. Mr. Radley joined C1 in October 2004 after working with Navigo Energy as Senior Engineer since June 2002. Previously, Mr. Radley worked for Nowsco Well Service, Alberta Energy Company, and NAL Resources on drilling, completions, production, facilities and reservoir engineering.

THE C1 TEAM

Our people contribute operations experience from major oil fields within sensitive areas, and operations in unique oil and gas areas requiring dedicated commitments to working with governmental, non-governmental, First Nations and aboriginal communities. C1's commitment to integrity in business and operations provides a competitive advantage in accessing new opportunities.

(LEFT TO RIGHT)

HUGH PATTILLO
PRESIDENT AND CHIEF EXECUTIVE OFFICER

GARY LOBB
VICE PRESIDENT OF FINANCE
AND CHIEF FINANCIAL OFFICER

JIM DITTRICH
CHIEF GEOPHYSICIST

(LEFT TO RIGHT)

STACEY RADLEY
MANAGER, ENGINEERING

KIM SOROCHAN
ENGINEERING TECHNOLOGIST

BILL VANDERVEEN
VICE PRESIDENT OF EXPLORATION

(LEFT TO RIGHT)

GARY CAMPBELL
LAND MANAGER

DEB SHIMEK
SUPERVISOR ACCOUNTING

RON BARMBY
VICE PRESIDENT AND
CHIEF OPERATING OFFICER

CORPORATE INFORMATION

BOARD OF DIRECTORS

Johannes (Jim) Nieuwenburg
Independent Businessman

Raymond Chan
President and Chief Executive Officer
Baytex Energy Trust

Ronald McIntosh
Independent Businessman

Kenneth McNeill
Independent Businessman

Christopher Nixon
Partner
Stikeman Elliott LLP

Hugh Pattillo
President and Chief Executive Officer
C1 Energy Ltd.

Herb Pinder
President
Goal Group of Companies

OFFICERS

Hugh Pattillo
President and Chief Executive Officer
C1 Energy Ltd.

Gary Lobb
Vice President of Finance
and Chief Financial Officer
C1 Energy Ltd.

Ron Barmby
Vice President and Chief Operating Officer
C1 Energy Ltd.

Bill VanderVeen
Vice President of Exploration
C1 Energy Ltd.

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National Bank of Canada

LEGAL COUNSEL

Burnet, Duckworth & Palmer LLP

RESERVES ENGINEERS

Sproule Associates Limited

TRANSFER AGENT

Computershare Investor
Services Inc.

EXCHANGE LISTING

Toronto Stock Exchange
Stock Symbol: CTT

ABBREVIATIONS

bbl(s)	barrel(s)
mbbls	thousand barrels
mmbbls	million barrels
mcf	thousand cubic feet
mmcf	million cubic feet
bcf	billion cubic feet
boe	barrel of oil equivalent (6 mcf = 1 bbl)
mboe	thousand boe/d per day
mmbtu	million British thermal units
NGLs	natural gas liquids
API	Alberta Petroleum Index
AMI	Area of mutual interest
ARTC	Alberta Royalty Tax Credit
FNR	Future net reveune
GPP	Good Production Practice
NPV	Net present value
JV	Joint Venture
RLI	Reserve Life Index
WTI	West Texas Intermediate

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